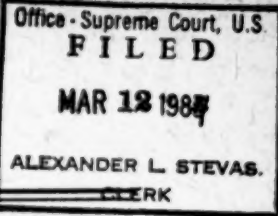


No. 83-1000



In the Supreme Court of the United States

OCTOBER TERM, 1983

J.D. COURT, INC., PETITIONER

v.

UNITED STATES OF AMERICA

*ON PETITION FOR A WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS FOR
THE SEVENTH CIRCUIT*

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

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TABLE OF AUTHORITIES

Page

Cases:

<i>Aetna Ins. Co. v. Texas Thermal Indus., Inc.</i> , 591 F.2d 1035	3
<i>Consolidated Film Industries v. United States</i> , 403 F. Supp. 1279, rev'd on other grounds, 547 F.2d 533	6
<i>Donald v. Madison Industries, Inc.</i> , 483 F.2d 837	5
<i>Manalis Finance Co. v. United States</i> , 442 F. Supp. 579, aff'd, 611 F.2d 1270	6
<i>Rice Investment Co. v. United States</i> , 625 F.2d 565	5
<i>Sgro v. United States</i> , 609 F.2d 1259	3, 5
<i>Texas Oil and Gas Corp. v. United States</i> , 466 F.2d 1040, cert. denied, 410 U.S. 929	5
<i>United States v. Kimbell Foods, Inc.</i> , 440 U.S. 715	5, 6

Statutes:

Internal Revenue Code of 1954 (26 U.S.C.):

§ 6321	1
§ 6323	1, 2, 3, 4, 5, 6
§ 6323(c)	6
§ 6323(c)(1)	3
§ 6323(c)(2)(B)	2, 3, 4
§ 6323(c)(2)(C)	4
§ 6323(h)(1)	4
§ 6331	2
§ 7426(a)(1)	2

II

Page

Miscellaneous:

H.R. Rep. 1884, 89th Cong., 2d Sess. (1966)	4, 5
S. Rep. 1708, 89th Cong., 2d Sess. (1966)	5

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Petitioner challenges the court of appeals' holding that, under Section 6323 of the Internal Revenue Code, federal tax liens had priority over petitioner's security interest in certain accounts receivable of a delinquent taxpayer. The decision below is correct and does not conflict with that of any other circuit. There is no basis for review by this Court.

1. Petitioner held a security interest in certain property of Eventide Homes, Inc., a nursing home (Pet. App. A2). Petitioner's security interest covered Eventide's "accounts receivable, * * * now or hereafter existing," and was perfected by a proper filing with the Illinois Secretary of State on May 17, 1979 (*id.* at A2-A3). Eventide became delinquent in the payment of its federal taxes. On September 17, 1979, the IRS, pursuant to Section 6321 of the Code,¹ filed

¹Unless otherwise noted, all statutory references are to the Internal Revenue Code of 1954 (26 U.S.C.), as amended (the Code or I.R.C.).

the first of several notices of tax lien against Eventide's property (*id.* at A4). The aggregate amount of delinquent taxes covered by these liens was \$68,925 (*ibid.*).

Between October 1979 and February 1980, Eventide furnished nursing care to Medicaid recipients (Pet. App. A2). Under the Medicaid program, Eventide was entitled to receive reimbursement in the amount of \$33,000 from the Illinois Department of Public Aid (*id.* at A3). Pursuant to Code Section 6331, the IRS issued a notice of levy to the Department, seeking to apply the \$33,000 against Eventide's delinquent taxes (*id.* at A3-A4).

Petitioner brought this wrongful levy action under Code Section 7426(a)(1) to test the relative priority of its security interest in, and the government's tax liens on, the \$33,000. The validity and priority of federal tax liens is governed by Section 6323. Section 6323(c)(2)(B) provides that, in the case of a "commercial transactions financing agreement," the lender's security interest has priority over a tax lien only if "[the] commercial financing security [is] acquired by the taxpayer before the 46th day after the date of tax lien filing." The government, citing this provision, contended that petitioner's security interest prevailed over the tax liens only to the extent that Eventide had "acquired" the accounts receivable—*i.e.*, earned them by performance of services—within 45 days of September 17, 1979, the tax lien filing date. Petitioner contended that its security interest prevailed over the tax liens as to all of Eventide's accounts receivable, regardless of when Eventide performed its services. The parties stipulated that, of the \$33,000 in question, \$907 represented amounts due Eventide for services rendered within the 45-day period, the balance representing amounts due for services rendered thereafter (Pet. App. A3-A4).

The district court agreed with the government, and the court of appeals unanimously affirmed (Pet. App. A1-A12). It reasoned that the tax liens were entitled to priority unless petitioner's competing security interest had become "choate" within 45 days of the lien filing date (*id.* at A6-A11). The court of appeals concluded that "a security interest in accounts receivable does not become 'choate' until the accounts receivable actually come into existence, that is, at the time the services giving rise to the accounts receivable are performed" (*id.* at A12, citing *Sgro v. United States*, 609 F.2d 1259, 1261 (7th Cir. 1979)). The court accordingly held that petitioner had priority only as to the accounts earned by Eventide's performance within the 45-day period, *i.e.*, only to the extent of \$907.

2. The decision below is correct. Although the court of appeals reached its result by applying the "choateness" doctrine, that same result could have been reached—more properly, in our view—by a straightforward application of the statutory language, without resort to notions of "choateness." As other courts have noted, "the 'choateness' rule of federal common law * * * has been supplanted by the provisions of [I.R.C.] § 6323 with respect to tax lien priority questions as to which that statute provides an unambiguous federal law answer." *E.g., Aetna Ins. Co. v. Texas Thermal Indus., Inc.*, 591 F.2d 1035, 1038 (5th Cir. 1979). The statute clearly offers "an unambiguous federal law answer" to the lien priority question posed here.

Section 6323(c)(1) generally provides that a federal tax lien, even though properly filed, is invalid "with respect to a security interest which came into existence after [the] tax lien filing," provided that the competing security interest is in "qualified property" covered by a "commercial transactions financing agreement." Section 6323(c)(2)(B) defines "qualified property" as being limited to "commercial financing security acquired by the taxpayer before the 46th day

after the date of [the] tax lien filing." Section 6323(c)(2)(C), as relevant here, defines "commercial financing security" to mean "accounts receivable."²

These statutory provisions unambiguously mandate the result reached by the court of appeals. Eventide ("the taxpayer") plainly did not "acquire" its accounts receivable (the "commercial financing security" involved here) until it performed the nursing-care services entitling it to reimbursement. Under Section 6323(c)(2)(B), therefore, the priority of petitioner's security interest, being limited to "qualified property," is limited to the accounts receivable Eventide earned by performing services "before the 46th day after the date of [the] tax lien filing."

The correctness of this analysis is confirmed by Section 6323(h)(1). That Section defines a "security interest" to exist only "at such time [as] the [underlying] property is in existence." The legislative history states that, "[f]or federal tax purposes, a security interest is not considered as existing until the conditions set forth [in Section 6323] are met even though local law may relate a security interest back to an earlier date and even though it might be an effective security interest as of the earlier date under the Uniform Commercial Code." H.R. Rep. 1884, 89th Cong., 2d Sess. 11-12

²Section 6323(c)(2)(C) defines "commercial financing security" also to include "paper of a kind ordinarily arising in commercial transactions." In the courts below, petitioner argued that it had a "commercial financing security" of this sort, on the theory that its security interest covered, not Eventide's accounts receivable, but Eventide's "contract rights" to receive payment from the Illinois Department of Public Aid. See Pet. App. A12 n.11. The court of appeals rejected this argument, holding that Eventide "was not obligated to provide services for public aid recipients," was entitled to payment only "if and when it chose to perform such services," and accordingly "had no 'contract right' to receive reimbursement * * * until such time as services were actually performed" (*ibid.*).

(1966).³ Congress's intention in enacting Section 6323 was to limit the priority of a competing security interest to property that was in existence at the time of tax lien filing, or that was acquired (*i.e.*, came into existence) within 45 days thereafter. H.R. Rep. 1884, *supra*, at 41-42; S. Rep. 1708, 89th Cong., 2d Sess. 7-8 (1966). Accord, *Texas Oil and Gas Corp. v. United States*, 466 F.2d 1040 (5th Cir. 1972), cert. denied, 410 U.S. 929 (1973); *Rice Investment Co. v. United States*, 625 F.2d 565 (5th Cir. 1980); *Donald v. Madison Industries, Inc.*, 483 F.2d 837 (10th Cir. 1973); *Sgro*, 609 F.2d at 1261. Since Eventide's accounts receivable were clearly not "in existence" until it performed the services requisite to earn them, petitioner's security interest had priority only as to those receivables earned by Eventide's performance within 45 days of the tax lien filing date.

3. Because the language of Section 6323, considered in isolation, unambiguously mandates the result reached by the court of appeals, this case does not require consideration of the question petitioner seeks to present—whether Congress "intend[ed] to curtail or abrogate the application of the federal judicial doctrine of choateness" by enacting Section 6323 (Pet. i, 5-11). Even if the statute could be considered ambiguous, however, the decision below, in invoking that doctrine, would still be correct. In asserting (Pet. 10-11) that there is "confusion * * * as to the viability of the [choateness] doctrine," petitioner relies chiefly on *United States v. Kimbell Foods, Inc.*, 440 U.S. 715 (1979). In that case, this Court held that state law, rather than federal common law with its "choateness" gloss, provides

³In light of this legislative history, petitioner's contention (Pet. 8) that the Uniform Commercial Code, as enacted by Illinois, defines "account" to include "any right to payment * * * for services rendered * * *, whether or not it has been earned by performance," is irrelevant to the lien priority question presented here.

the rule of decision in ascertaining the relative priority of a perfected private security interest and a competing federal lien, where the federal lien arises out of a federal contract. 440 U.S. at 727-729.

The court of appeals correctly held (Pet. App. A9-A11) that the "choateness" doctrine—to the extent resort to it is necessary—continues to have vitality in considering the priority of a federal tax, rather than a federal contractual, lien. This Court in *Kimbell Foods* carefully distinguished between the government's activities as contractor and tax collector, emphasizing that prompt collection of taxes "is vital to the functioning, indeed existence, of government" and that the need for prompt revenue collection justifies "the extraordinary safeguards applied in the tax lien area" (440 U.S. at 734, 735). The Court likewise stressed (*id.* at 718, 735) that the contractual liens involved in *Kimbell Foods* were not subject to any federal statute that "established a priority scheme displacing state law" (*id.* at 735). In the present case, by contrast, Congress has established in Section 6323(c) a specific priority scheme to be used in resolving conflicts between accounts receivable financing arrangements and federal tax liens. To the extent Section 6323's operation is ambiguous, Congress surely intended that its language should be supplemented, not by variegated state-law rules, but by uniform principles derived from federal common law. Nothing in *Kimbell Foods* suggests a different result—indeed, this Court specifically declined (440 U.S. at 735 n.34) to reach the question—and there is no conflict of decision on the issue in the courts of appeals.⁴

⁴Contrary to petitioner's assertion (Pet. 11), neither *Manalis Finance Co. v. United States*, 442 F. Supp. 579 (C.D. Cal. 1977), *aff'd*, 611 F.2d 1270 (9th Cir. 1980), nor *Consolidated Film Industries v. United States*, 403 F. Supp. 1279 (D. Utah 1975), *rev'd* on other grounds, 547 F.2d 533 (10th Cir. 1976), conflicts with the decision below. Neither case considered the applicability of the "choateness" doctrine where a federal tax lien was concerned.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

REX E. LEE
Solicitor General

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